

Under Illinois law, lessors under true lease agreements are deemed the users of items they purchase for rental purposes. Accordingly, lessors incur a Use Tax liability on such purchases. See 86 Ill. Adm. Code 130.2010. (This is a GIL).

June 25, 2002

Dear Xxxxx:

This letter is in response to your letter that we received on April 2, 2002. The nature of your letter and the information you have provided require that we respond with a General Information Letter, which is designed to provide general information, is not a statement of Department policy and is not binding on the Department. See 2 Ill. Adm. Code 1200.120(b) and (c), which can be accessed at the Department's Website at <http://www.revenue.state.il.us/Laws/regs/part1200/>.

In your letter, you have stated and made inquiry as follows:

I am writing in regards to the sales tax treatment on commissions as they pertain to our lease agreements. AAA buys the tangible personal property from our vendors and in turn lease it to businesses located in your state. Our standard lease period is for 36 months and can have residuals of fair market value, 10% of the equipment cost, \$1.00, or no buyout at all (a true rental agreement).

On occasion, AAA will be billed by our vendors a commission. We consider any money paid to the vendor as part of the equipment cost, but if some of our vendors bill us for sales tax they do not include the commission as part of the sales tax basis. If the lease needs to have sales tax paid upfront, whether by the vendor or AAA, or billed on each monthly rental stream, is the commission part taxable?

Going forward, AAA would like to know the correct way to handle this. Please respond with a legal opinion so we can provide this information to the vendor as needed to correct any sales tax issues. I have enclosed a copy of our lease agreement for your review. Please contact me if you have any questions or need further explanation on any details. Thank you for your time and cooperation.

For general informational purposes we enclose a copy of 86 Ill. Adm. Code 130.2010, the Department's regulation that covers the taxation of leases. Under Illinois law, "true leases" and "leases" that are actually conditional sales contracts are treated differently for Retailers' Occupation and Use Tax purposes. Lessors are subjected to a Use Tax on their cost price of tangible personal property that they acquire to use by leasing under true leases in Illinois. This means lessors in Illinois encounter a front-end tax on value rather than an amortized tax on receipts. The only exception is automobiles rented for one year or less, which are subject to the Automobile Renting and Use Tax found at 35 ILCS 155/1 et seq.

True leases generally have no buy out provisions at the close of the leases. If buy out provisions do exist, they must be fair market value buy out options in order to maintain the character of the true leases. Lessors of tangible personal property under true leases in Illinois are deemed end users of the property to be leased. See, 86 Ill. Adm. Code 130.220(a). As end users of tangible personal property located in Illinois, lessors incur Use Tax liability on their cost price of such property. Except for short-term automobile rentals, there is no tax due upon rental receipts in Illinois.

Under Section 130.2010(a), persons who purport to "lease" the use of property, but in fact sell such tangible personal property to nominal "lessees," are considered to be making conditional sales subject to Retailers' Occupation Tax. Such would be the case when the agreements contain nominal purchase options at the end of the lease term. In these situations Retailers' Occupation Tax is due on all the payments received by the "lessors."

The lease appended to your letter shows that you and your customer may choose either a \$1.00 or a fair market value purchase option at lease end. As noted above, the latter would designate the agreement as a true lease while the former would mean the agreement is a conditional sale, with tax due upon all payments received by your company. Your lease agreement also contains a possible purchase option for a designated percentage of cost. If this purchase option is part of the agreement and it is for an amount that approximates fair market value, then the agreement would be a true lease. If the amount were to be nominal, then the agreement would be a conditional sale.

For true leases where the lessor owes tax up front on the cost price, a commission is a cost of doing business that is subject to tax. Please refer to 86 Ill. Adm. Code 130.410, enclosed. The treatment of commissions you pay to your vendor may or may not be taxable under your conditional sales agreements. In conditional sales situations, vendor commissions can be excluded from the tax calculation so long as they are not included in the selling price of the items being sold. However, if you pass them on to your customers as part of your selling price, they would be subject to tax.

I hope this information is helpful. The Department of Revenue maintains a Web site, which can be accessed at www.revenue.state.il.us. If you have further questions related to the Illinois sales tax laws, please contact the Department's Taxpayer Information Division at (217) 782-3336.

If you are not under audit and you wish to obtain a binding Private Letter Ruling regarding your factual situation, please submit all of the information set out in items 1 through 8 of Section 1200.110(b).

Very truly yours,

Karl W. Betz
Associate Counsel

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